

***United States Court of Appeals  
for the Second Circuit***



**PETITIONER'S  
REPLY BRIEF**





# 77-4078

To be argued by  
WILLIAM E. WILLIS

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## United States Court of Appeals

For the Second Circuit

Docket No. 77-4078

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SCM CORPORATION,

*Petitioner,*

—against—

FEDERAL TRADE COMMISSION,

*Respondent.*

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ON PETITION FOR REVIEW OF A  
FINAL ORDER OF THE FEDERAL TRADE COMMISSION

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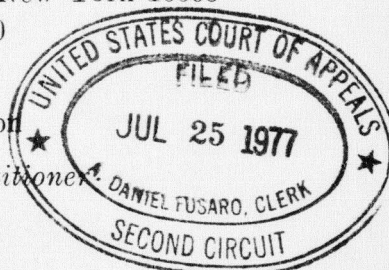
### REPLY BRIEF FOR PETITIONER

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# United States Court of Appeals

For the Second Circuit

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SCM CORPORATION,

*Petitioner,*

—against—

FEDERAL TRADE COMMISSION,

*Respondent.*

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## REPLY BRIEF FOR PETITIONER

The most striking aspect of the Federal Trade Commission's ("FTC" or "Commission") brief is its repeated insistence that the Commission's administrative discretion entitles it to issue an injunction without any showing that there is a danger of a future violation of the law. Similarly, the Commission invokes "discretion" as its purported justification for imposing, without a valid explanation for so doing, a substantially harsher cease and desist order on one of several identically situated respondents. Finally, the Commission asks this Court to defer to its construction of Section 8 of the Clayton Act, 15 U.S.C. § 19, and Section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, on the ground that Congress has given it discretion to administer these statutes.

The fact remains, however, that no administrative agency has discretion to define the law contrary to the language of the statute it claims to be enforcing, to enforce the



law contrary to well established standards for awarding injunctive relief, or to apply the law to individual respondents in derogation of basic principles of due process and equal protection. The present case is one in which the FTC has erred as a matter of law. SCM Corporation ("SCM"), therefore, asks this Court to relieve it of a cease and desist order unauthorized by Section 8 and predicated upon errors of law and the arbitrary exercise of administrative discretion.

# I.

## The Standard for Injunctive Relief

It is clear from the FTC's brief<sup>1</sup> that the Commission has misconstrued the thrust of SCM's argument that the Staff failed to meet its burden of proof to support an award of injunctive relief. In its principal brief (SCM Br. 9-18), SCM argued that the Commission used an incorrect standard of law in issuing a cease and desist order and failed to present any evidence that SCM was likely to violate the law in the future. SCM argued that the correct standard was articulated by the Supreme Court in *United States v. W. T. Grant Co.*, 345 U.S. 629, 633 (1953) ("some cognizable danger of recurrent violation"). In response, the Commission took the position that "[t]he FTC [d]id [n]ot [a]buse [i]ts [d]iscretion" (emphasis added) and that "[t]he only proper issue before this Court concerning remedies is whether the FTC has made 'an allowable judgment in [its] choice of remedies.'" (FTC Br. 21).

<sup>1</sup>References to ("SCM Br. —") and to ("FTC Br. —") refer to pages in SCM's and the FTC's principal briefs respectively. As in its principal brief, SCM will continue to use the designation ("A—") to refer to pages in the Joint Appendix.



Having framed the issue as one involving "discretion", the Commission has simply missed the point. There is no *discretion* as to the applicable standard for injunctive relief in Section 8 cases. That standard was established in *Grant, supra*: "The necessary determination is that there exists some cognizable danger of recurrent violation. . . ." As demonstrated in SCM's principal brief (SCM Br. 10), the Commission failed to apply that standard in imposing a cease and desist order on SCM but substituted its own standard of a "possibility of future such occurrences" (A160)—a standard specifically rejected by the Supreme Court in *Grant*. Once it is recognized that the Commission erred as a matter of law<sup>2</sup> in applying an erroneous standard for injunctive relief, it becomes unnecessary to reach the secondary question (focused upon by the Commission in its brief) of the scope of the FTC's discretion in fashioning an equitable remedy in a particular case. The latter issue, along with the cases cited by the Commission for the proposition that courts will not interfere with its choice of remedies, presumes initial application of the correct standard of law, which was not the case here.<sup>3</sup>

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<sup>2</sup> Because it framed the issue as to the correct standard for injunctive relief as one of discretion rather than as a question of law, the Commission further erred in arguing that "the Court's review is narrowly restricted." (FTC Br. 21). In fact, the applicable standard of review is the broad one of "error as a matter of law." *SEC v. Chenery Corp.*, 318 U.S. 80, 94 (1943). See generally, SCM Br. 7-8.

<sup>3</sup> That the Commission has consistently put the cart before the horse by focusing on the form of relief it is empowered to issue rather than the need for any injunctive relief is evidenced in the statement appearing on page 6 of the FTC's brief: "When asked by the ALJ how SCM's business would be affected by the contemplated relief, SCM's counsel was unable to point out any adverse impact other than a 'feel[ing]' by the directors that 'a reporting

While the Commission failed squarely to address SCM's argument that it had applied an erroneous standard for injunctive relief, several of the points made in its brief emphasize the extent to which the Commission did in fact apply an erroneous standard in this case.

(1) The Commission continues to insist that a respondent bears the burden of proving that injunctive relief is unnecessary. (FTC Br. 23 n.19). It tries to support this untenable position by a tortured attempt to distinguish the *Grant* case and by citation to *United States v. Concentrated Phosphate Export Assn.*, 393 U.S. 199 (1968). (FTC Br. 23 n.19). The *Grant* case speaks for itself: "[T]he moving party must satisfy the court that relief is needed." 345 U.S. at 633. *Accord, Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 63 (1975). *Grant's* articulation of the standard for injunctive relief cannot be distinguished away, as the Commission attempts to do, on the ground that it arose from a district court's denial of injunctive relief which the Supreme Court, *after defining the standard for injunctive relief*, upheld as a proper exercise of discretion on the facts of that case. The *Concentrated Phosphate* case has already been discussed in SCM's principal brief (SCM Br. 13 & n.8) and need not be extensively analyzed here. Suffice it to say that *Concentrated Phosphate, supra*,

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restriction' would be 'a burden' (A186-87)". Putting aside the fact that this quotation is taken out of context (counsel actually said "this [reporting restriction] is a burden which [the directors] feel, under the law, is not appropriate in this case . . ."), the question that the Commission should have focused upon, but didn't, is what evidence exists to prove that injunctive relief is warranted. Instead, the Commission improperly reasoned that a cease and desist order issues automatically, absent a showing by SCM that injunctive relief is unnecessary (*e.g.*, because it would peculiarly burden SCM).



deals with the burden of proving mootness as an affirmative defense, not with the burden of proving the need for injunctive relief.<sup>4</sup>

(2) The Commission argues that *Rondeau, supra*, and *SEC v. Management Dynamics, Inc.*, 515 F.2d 801 (2d Cir. 1975) are inapposite. (FTC Br. 25). That the Commission fails to perceive the relevance of these cases is but one illustration that it has misconstrued the thrust of SCM's argument (attacking the FTC's use of an erroneous standard for injunctive relief and consequent failure to present evidence of the need for an injunction against SCM). As set forth in SCM's principal brief (SCM Br. 13-16), not only does *Rondeau* adopt verbatim the "cognizable danger of recurrent violation" standard of *Grant*, 422 U.S. at 59, but it categorically rejects the holding of the Commission that proof of a past violation is sufficient in itself to support an award of broad prospective injunctive relief. *Compare*, the Commission's Opinion: "[W]e think the violation is itself the best evidence of the possibility of future such occurrences, and that the burden rests with respondent to demonstrate that violations will not recur before consideration may be given to omitting an order," (A160); *with*, the Supreme Court's rejection of the identical argument in *Rondeau*, 422 U.S. at 60, *and* this Court's language in *Management Dynamics*,

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<sup>4</sup> It is surprising that the Commission cites *Concentrated Phosphate, supra*, and never mentions SCM's argument that the case "says nothing about what a plaintiff must show to obtain injunctive relief." (SCM Br. 13). Indeed, the Commission appears to concede this point when, in describing what the Supreme Court did in that case, it wrote, "the Court rejected a *mootness* argument." (Emphasis added) (FTC Br. 23 n. 19). It is significant that the Commission had no other authority to cite for its erroneous proposition that a respondent bears the burden of proving that injunctive relief is unnecessary.



"illegal activity, without more, does not automatically justify issuance of an injunction." 515 F.2d at 807.<sup>5</sup>

While the Commission could say nothing in its brief that would alter the fact that it applied an erroneous standard of law in issuing a cease and desist order against SCM (A160), it has attempted retroactively to demonstrate that it did have record evidence to support an award of injunctive relief. Specifically, the Commission cites four "facts" that it allegedly considered.

The first "fact" that the Commission points to as evidence of the need for an injunction is "that the interlock had continued for several years and was terminated only after the Commission had acted." (FTC Br. 22). It need hardly be stated that the duration of a past violation is not, in itself, evidence "that there exists some cognizable danger of recurrent violation" (*Grant*, 345 U.S. at 633)—the only inquiry relevant to determining the need for prospective injunctive relief. It is particularly inapposite in this case where the Commission itself recognized that SCM's past violation was not intentional. (A158). Moreover, in observing that the offending interlock was terminated "only after the Commission had acted", the Commission neglects to mention that SCM, as distinguished from all previous Section 8 respondents since at least 1960,

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<sup>5</sup> The Commission cites several cases in support of the proposition that "the FTC Act [and] the Clayton Act . . . permit the Commission to issue cease and desist orders upon finding that a person has committed illegal acts, even if the illegal conduct has ceased." (FTC Br. 25-26). Suffice it to say that none of these cases holds that an injunction can be predicated on a violation alone. Here, SCM acknowledged at the outset of its principal brief (SCM Br. 4) that Bond's resignation does not require that the FTC's complaint be dismissed as moot but does merit consideration as a factor tending to show that prospective injunctive relief is unnecessary.

was not given an opportunity prior to issuance of a formal complaint to effectuate voluntary compliance and that, once SCM and the offending director were notified of the Commission's investigation, the director voluntarily resigned within 10 days.

The second "fact" which the Commission now claims that it considered in issuing an injunction against SCM was that "competition between Krafteo and SCM involved more than \$300,000,000 in Krafteo sales and more than \$80,000,000 in SCM sales." (FTC Br. 22). How the dollar volume of SCM's sales in competition with Krafteo demonstrates the need for prospective injunctive relief is not readily apparent. What this fact is relevant to is proof of a violation of Section 8—that the corporations sharing a common director have "capital, surplus, and undivided profits aggregating more than \$1,000,000." But, as discussed *in extenso* in SCM's principal brief (SCM Br. 14-16), since the fact of a violation is insufficient without more to justify prospective injunctive relief, a subsidiary fact (the dollar volume of sales in competition) relevant only to proof of a violation is *a fortiori* insufficient to support issuance of an injunction.

The third "fact" which allegedly supports a cease and desist order against SCM is "the narrow, and unenforceable, promise that SCM had made concerning Bond and its failure to make any promise concerning other unlawful interlocks." (FTC Br. 22). This observation by the Commission is both false and misleading. SCM offered the Commission voluntary assurances of future compliance with Section 8 by affidavit on November 16, 1975, seven months before the Administrative Law Judge's initial decision. As to the scope of SCM's promise, the words of the representation speak for themselves: "... Mr. Bond will



not be re-elected to the Board of Directors of SCM so long as he is a director of Kraftco *or any corporation which competes or might compete in any line of commerce with SCM.*" (Emphasis added) (Sexton Aff., para. 10, A32-33). The Staff never requested a broader representation from SCM or even suggested that it would recommend any settlement short of the broad cease and desist order that ultimately issued. Under such circumstances, the Commission should not be permitted to pervert SCM's good faith attempt to resolve this matter informally into "evidence" of the need for prospective injunctive relief.

Finally, the Commission cites as a predicate for injunctive relief, "SCM's failure to inform the Commission of any corrective steps it had taken or would take." (FTC Br. 22). Suffice it to say that the Staff's obstinate refusal to consider resolution of this matter by any means other than a cease and desist order made it futile for SCM even to discuss with the Staff voluntary representations broader than the one given on November 16, 1975, or the details of a voluntary plan to avoid future inadvertent interlocks. The Staff's decision to block all meaningful discussions which might have led to further voluntary representations by SCM cannot now be converted into "evidence" that SCM is an intractable law violator that refused to assure the Commission that it had taken "corrective steps" and, therefore, must be subjected to a broad cease and desist order.

None of the four "facts" cited by the Commission in its brief constitutes affirmative evidence "that there exists some cognizable danger of recurrent violation." (*Grant*, 345 U.S. at 633). Indeed, that the Commission went to the trouble of mentioning these "facts" at all indicates its tacit



recognition, despite its argument to the contrary, that something more than evidence of a past violation is required to sustain prospective injunctive relief. Here, the administrative record is devoid of any such evidence. It is too late for the Commission to cure this deficiency and it must not be permitted to obscure it by the clever manipulation of record "facts" which, viewed in their proper context, provide no support for issuance of an injunction against SCM.

Even if these so-called "facts" could be considered as evidence of a need for injunctive relief, the cease and desist order against SCM must be vacated because the Commission assessed these facts in light of an erroneous view of the controlling law. The Commission never weighed these "facts" to determine if they satisfied *the Staff's burden* of proving that injunctive relief is necessary. The Supreme Court has made it clear that an order predicated upon an error of law cannot stand regardless of the "facts" later recited in the administrative agency's brief.

"But even if the findings were considered to be adequate foundation for an opinion and order . . . , they still fail to sustain the Commission action; for the Commission has not rendered an opinion which, by the route suggested, links its findings and its conclusions. . . . Our view is that 'the considerations urged here in support of the Commission's order were not those upon which its action was based.' *SEC v. Chenery Corp.*, 318 U.S. 80, 92 (1943). . . . The Commission's action being flawed in this respect, we cannot sustain its order." *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 248-49 (1972).

*Accord, National Association of Women's and Children's Apparel Salesmen, Inc. v. FTC*, 479 F.2d 139, 147 (5th Cir.), *cert. denied*, 414 U.S. 1004 (1973) ("A fundamental

principle of judicial review of administrative action requires that in order for a reviewing court to sustain agency action the legal grounds upon which the agency acted must be correct.")

## II.

### Section 8 of the Clayton Act

Since the Commission's discussion of Section 8 of the Clayton Act in its brief (FTC Br. 11-18) consists primarily of a repetition of the discussion found in its Opinion (A151-155), SCM will rely primarily upon the analysis presented in its principal brief. (SCM Br. 18-24). However, several of the points raised in the Commission's brief are so misleading or erroneous as to require specific response.

(1) In arguing that Section 8 imposes liability on corporations as well as individual directors, the Commission places primary reliance on its interpretation of Section 11 of the Clayton Act, 15 U.S.C. § 21. That section authorizes, among other forms of relief for a violation of the Act, a cease and desist order requiring the respondent to "rid itself of the directors chosen contrary to the provisions of [Sections 7 and 8 of this Act]." Reasoning that "only a corporation may 'rid itself' of directors," (A153 and FTC Br. 14), the Commission concludes that Section 8 imposes substantive liability on corporations.

It is surprising that the Commission repeats in its brief the same Section 11 analysis found in its Opinion without even addressing SCM's arguments that the procedural provisions of Section 11 cannot be used to create substantive liability under Section 8 and that the "rid itself"



language of Section 11, read in light of the Clayton Act's legislative history, is nothing more than a vestigial remainder. (SCM Br. 22-23). Nor does the Commission come to grips with the logical consequence of its own argument—that any Section 11 order against a corporation having an individual director in violation of Section 8 is limited by the very language of Section 11 to requiring the corporation to “rid itself” of the offending director. And, since Bond resigned from SCM's board on August 1, 1975, there is no basis for a “rid itself” order against SCM.

(2) The Commission claims that its decision “has substantial judicial support.” (FTC Br. 15). In light of the paucity of cases involving Section 8 and the Commission's citation to only two cases which allegedly support its position, the suggestion that there is “substantial judicial support” for the proposition that corporations, as distinguished from individual directors, are subject to substantive liability under Section 8 is wholly unwarranted.<sup>6</sup>

The two district court cases cited by the Commission can hardly be considered as judicial support for its position. In *United States v. Sears, Roebuck & Co.*, 111 F. Supp. 614 (S.D.N.Y. 1953), the issue of whether a corporation is subject to substantive liability under Section 8 was not even discussed. It is noteworthy that the Commission's quotation from this case comes not from Judge Weinfeld's principal opinion but from a brief supplementary opinion denying injunctive relief. The passage cited by the Commission (“The violation of the statute was committed by the individual defendant in accepting

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<sup>6</sup> The Commission does note that the Supreme Court reserved judgment on the issue in *Grant*, 345 U.S. at 634 n.9.



membership on the Boards of Directors of both corporations and by the latter in acquiescing therein over an extended period of years"—(FTC Br. 15)) appears as a one sentence description of the case before the operative sentence denying injunctive relief. [1952-53] Trade Cases (CCH) ¶ 67,561. Such a casual statement, without analysis and made in a context in which Section 8's applicability to corporations was not at issue, can hardly be deemed "substantial judicial support" for the Commission's present argument.<sup>7</sup> Nor does Judge Weinfeld's further opinion in the *Sears* case, 165 F. Supp. 356, focus on the substantive liability of corporations under Section 8. Indeed, the Court's language in that opinion can be read to contravene the Commission's position:

"The provisions of the decree are not limited to the language of Section 8 of the Clayton Act which by its terms is applicable to *directors* of corporations engaged in competition." (Emphasis added) (165 F. Supp. at 358).

Besides exaggerating the significance of the *Sears* case as judicial support for its argument, the Commission has wholly misinterpreted *United States v. Crocker National Corp.*, 422 F. Supp. 686 (N.D. Cal. 1976). That case lends

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<sup>7</sup> It is ironic for the Commission to cite the first sentence of Judge Weinfeld's supplementary opinion in the *Sears* case and fail to mention the second sentence which is so apt to SCM's argument, *supra* Point I, that injunctive relief should not issue absent proof of the danger of a recurrent violation.

"However, the broad injunction proposed against future violations of the statute should be granted only where there is evidence showing a persistent purpose to violate or commit recurrences of the condemned act. No such proof has been submitted to me. See *Hecht Company v. Bowles*, 321 U.S. 321, 329." [1952-53] Trade Cases (CCH) ¶ 67,561 (S.D.N.Y. 1953).

no support to the Commission's argument as the Court reserved decision on the question of whether Section 8 applies to corporations as well as individual directors. *Crocker National Corp.*, 422 F. Supp. at 705-06.<sup>8</sup> Thus, despite the Commission's vain efforts to cloak its position in the veil of prior judicial approval, the fact remains that whether Section 8 applies to corporations as well as to individual directors is an issue of first impression for resolution by this Court.<sup>9</sup>

(3) The Commission's final argument for adopting its interpretation of Section 8 (that corporations as well as individual directors are subject to substantive liability under that section) is based upon its claimed administrative expertise. The Commission points to the fact that it has in the past issued Section 8 complaints against corporations and has extracted from them "voluntary action [and] consent agreements. . . ." (FTC Br. 17 and n.14). Therefore, the Commission concludes, this Court should defer to its interpretation of the scope of Section 8, as the FTC is one of the agencies entrusted with enforcing that statute.

While there is no doubt that an agency's interpretation of the statute it administers merits weight (*e.g.*, *Udall v.*

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<sup>8</sup> One reason why the Court commented that it was empowered to issue an injunction against the defendant corporations under Section 11 was because the defendants so conceded at oral argument. 422 F. Supp. at 706.

<sup>9</sup> In a footnote to its analysis of *Crocker National Corp.*, *supra*, the Commission advances a confusing argument which, according to the Commission, leads to the conclusion that "SCM practically concedes the Section 8 issue." (FTC Br. 16 n.12). Not only is such a conclusion incorrect but it evidences the Commission's lack of comprehension of SCM's Section 11 argument. (See SCM Br. 23-24)



*Tallman*, 380 U.S. 1, 16 (1965)), it certainly does not end the issue. As the Supreme Court wrote:

"The construction put on a statute by the agency charged with administering it is entitled to deference by the courts, and ordinarily that construction will be affirmed if it has a 'reasonable basis in law.' [Citations omitted]. But the courts are the final authorities on issues of statutory construction [citation omitted] and 'are not obliged to stand aside and rubber-stamp their affirmance of administrative decisions that they deem inconsistent with a statutory mandate or that frustrate the congressional policy underlying a statute.' [Citation omitted]. 'The deference owed to an expert tribunal cannot be allowed to slip into judicial inertia. . . ." [Citation omitted]." *Volkswagenwerk Aktiengesellschaft v. Federal Maritime Commission*, 390 U.S. 261, 272 (1968).

Here, the issue of the scope of Section 8's applicability has never been squarely ruled on by a Court. Under such circumstances it would be improper simply to defer to the FTC. The fact that the FTC has subjected corporate respondents to Section 8 orders in the past is, in the absence of any judicial ruling on the question, as demonstrative of a history of the Commission's overstepping the statutory mandate as it is of a consistent record of enforcing Section 8 in conformity with Congressional intent. In *Federal Maritime Commission v. Seatrain Lines, Inc.*, 411 U.S. 726, 745 (1973) the Supreme Court wrote:

"But the Commission contends that since it is charged with administration of the statutory scheme, its construction of the statute over an extended period should be given great weight. [Citation omitted]. This proposition may, as a general matter, be conceded, *although*



*it must be tempered with the caveat that an agency may not bootstrap itself into an area in which it has no jurisdiction by repeatedly violating its statutory mandate."* (Emphasis added).

### III.

#### Section 5 of the Federal Trade Commission Act

While the arguments relating to Section 5 presented by the Commission in its brief (FTC Br. 18-21) have already been dealt with in SCM's principal brief (SCM Br. 25-30), two points bear mentioning.

(1) While it is true that the Commission has been accorded broad discretion under Section 5, *e.g.*, *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233 (1972), many of the cases in which the Commission's exercise of that discretion has been upheld have involved the classic cases of deceptive advertising and other unfair trade practices left unregulated except by Section 5(a)(1). SCM submits that the permissibility of broad discretion in such areas is far different than in situations, like the present case, where the allegedly "unfair or deceptive acts or practices" are already comprehensively regulated by statute (Section 8). There is much less room for discretion when the exercise thereof trenches upon legislative choices as to who is and who is not to be subjected to substantive liability.

(2) Should this Court, for any reason, conclude that Section 5 applies to a corporation having an individual director in violation of Section 8, the Commission's cease and desist order against SCM must still be vacated. The Commission's discretion under Section 5, no matter how sweeping, is not so broad as to legitimize issuance of an injunc-

tion without an affirmative showing by the moving party (here, the FTC) of a need for prospective injunctive relief. The Commission's failure to make such a showing, regardless of whether it was proceeding under Section 8, Section 5 or both, leaves this Court no alternative but to grant SCM's petition for review, to vacate the Commission's cease and desist order and to dismiss the FTC's complaint.

#### IV.

##### **Discriminatory Enforcement of Section 8**

The facts are clear: the FTC has discriminated against SCM in failing to accord it an opportunity to resolve the Commission's complaint informally and by imposing upon it a more burdensome order than it imposed upon the other respondents in the same proceeding.

##### **A. *The Commission's Investigation of SCM***

In its principal brief (SCM Br. 31-36), SCM presented facts, based upon the Stipulated Record (A62-116), demonstrating that SCM was the first corporation since at least 1960 to be subjected to a Part III, formal complaint without first having been accorded, under Part II of the Commission's Rules, an opportunity to negotiate an informal disposition of the matter. Additionally, SCM was virtually the only Section 8 respondent not given notice, in advance of issuance of a formal complaint, that it was being investigated. Therefore, SCM was completely deprived of an opportunity to effect voluntary compliance with Section 8 before the Commission's formal complaint issued. And after the complaint issued, the Staff absolutely refused to consider any resolution of this matter that did not include a broad cease and desist order.

It is significant that the Commission, in its answering brief, does not challenge the basic facts on which SCM's discrimination argument is based. Rather, the Commission raises in defense several arguments which, when analyzed, leave intact SCM's assertion that it was prejudiced by the Commission's conduct.

(1) The Commission argues that there was "nothing improper in the . . . change of its Rules of Practice and SCM was, like Kraftco and Bond, accorded a full opportunity to settle this matter by consent order after the complaint had issued." (FTC Br. 29-30). While a change in rules of procedure is not *per se* improper, it becomes so when it operates to the detriment of a respondent in an on-going investigation and when the change is implemented in derogation of the Commission's own statement of policy accompanying the change.

As discussed in greater detail in SCM's principal brief (SCM Br. 33-34), the FTC changed its Rules of Practice on April 4, 1975. 40 Fed. Reg. 15235. The Commission's investigation of SCM had commenced at least as early as March 7, 1975, at which time it was standard procedure for the Commission to utilize Part II of its Rules of Practice under which the Commission would issue a "proposed complaint" "for the purpose of encouraging consent settlements before a formal complaint was issued." (Initial Decision, p. 12 n.21, A130). By conveniently changing its rules in the middle of its investigation of SCM, the Commission deprived SCM of notice that an investigation was pending and an opportunity to negotiate an informal disposition before issuance of a formal complaint. Since the Staff, after issuance of the formal complaint, adamantly refused to consider resolving the case on any basis other



than a broad cease and desist order, litigation ensued. Then, the Commission, in its Opinion (A163), relied upon the fact that SCM did not settle as a basis for imposing on it a more severe cease and desist order—reasoning that SCM could be penalized because the Commission had to spend time and money in proving its case that would have been saved if this matter had been resolved at an early stage in the proceedings. Clearly, any change in Rules of Practice which leads to such an unfair impact on a respondent cannot be sanctioned.<sup>10</sup>

It is particularly ironic for the Commission now to contend that it is unimportant that SCM was not given an opportunity, prior to issuance of a formal complaint, to negotiate an informal disposition of this case. In its own statement of policy accompanying the April, 1975, rule change, the Commission wrote:

“This decision [to issue Part III complaints following future investigations] does not affect the Commission’s policy of encouraging settlements and discouraging litigation where a consent agreement is in the public interest. Opportunity to negotiate such agreements will continue to be available during the investigative stage, and, in appropriate circumstances, after complaint has issued.” 40 Fed. Reg. 15235.

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<sup>10</sup> Even in its brief on this petition for review, the Commission still seeks to derive unfair advantages from its self-serving rule change in April of 1975. The Commission cites as one reason why an injunction should issue the fact, “that the interlock . . . was terminated only after the Commission had acted.” (FTC Br. 22). Of course, it was the Commission’s decision not to proceed under Part II and, therefore, not to notify SCM that an investigation was pending that made it impossible for SCM or Bond to terminate the interlock before issuance of the FTC’s formal complaint. This, however, the Commission omits to mention.

It is clear, therefore, that in addition to prejudicing SCM by resulting in a more severe cease and desist order, the Commission's conduct of this investigation was in flagrant disregard of its own stated policy.

(2) The Commission has made much of a statement found in an affidavit by SCM's counsel to the effect that settlement was "an alternative which is not now and has not, at any time, been acceptable to SCM." (FTC Br. 30, citing Paul Aff., para. 5, A35). To quote this fragment of a sentence, without any reference to the context in which this statement was made, and to suggest that, because of this quotation, "SCM should not now be heard to argue that it has been prejudiced by the imaginary denial of an opportunity of which it never desired to avail itself" is grossly to distort the facts.

Miss Paul was reacting to the high handed approach of the Commission in attempting to use an alleged technical default by SCM as a club to make SCM submit to acceptance of a broad cease and desist order. Incredibly, the Staff's position on that motion was that depositing SCM's answer in the mail on the appointed date to answer was inadequate service and that the answer should have been filed in the office of the Secretary to the Commission on that date.<sup>11</sup> It was in this context that the Paul Affidavit recites the following language from which the Commission extracted the words it deemed useful to its argument.

"5. I received a copy of the instant motion on Friday, November 21, 1975 and telephoned complaint

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<sup>11</sup> The Administrative Law Judge rejected the Staff's frivolous argument by order of November 21, 1975. Presumably, however, the time and money spent by the Commission on this wasteful motion was also charged against SCM in the form of a more severe cease and desist order. (A163).



counsel, Clinton Batterton, to discuss the matter. He informed me at that time that it was his position that SCM's answer was due at the office of the Secretary on November 17, and refused to discuss the matter further, although he expressed a willingness to discuss terms of a consent decree between SCM and the Commission, an alternative which is not now and has not, at any time, been acceptable to SCM for reasons set forth in SCM's motion for summary decision." (Paul Aff., para. 5, A35).

Viewed in its proper context, all that the Paul Affidavit states is that SCM was unwilling to accept a "consent decree" (i.e., a broad cease and desist order) which, as discussed in SCM's principal brief (SCM Br. 35) and *supra*, was the only disposition that the Staff would consider after the formal complaint issued. To suggest, as does the Commission (FTC Br. 30), that SCM was unwilling to consider any informal resolution of this case is patently false and belied by the fact that SCM, seven months before issuance of the ALJ's Initial Decision, voluntarily proffered representations of future compliance with Section 8 as a basis for an informal disposition of this matter. (Sexton Aff., para. 10, A32-33).<sup>12</sup> In short, the Commission's reference to its carefully excerpted portion of the Paul Affidavit is nothing more than a bald attempt to muddy the waters and thereby obscure the serious import of SCM's discrimination argument.

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<sup>12</sup> It is noteworthy that resolution of Section 8 complaints on the basis of voluntary assurances was not new to the FTC. For years the FTC and the Justice Department were willing to accept such voluntary assurances and the Commission has cited no instance in which any respondent improperly took advantage of that situation.



**B. *The Disparity Between the SCM and Kraftco Orders***

At the outset of its attempt to justify the disparity among the SCM, Kraftco and Bond orders, the Commission makes the amazing statement that "[t]he prohibition against Kraftco is merely expressed in different language than the prohibition against SCM." (FTC Br. 27 n.21). SCM respectfully refers this Court to the comparative analysis of the three orders in SCM's principal brief. (SCM Br. 37-38). That the orders are substantively different is readily apparent. Indeed, in its Opinion (A161-164) the Commission spends four pages justifying its order and articulating reasons, however constitutionally infirm, why the SCM order could be more severe than the Kraftco order. Under such circumstances, the Commission's suggestion in its brief that there are no real differences between the Kraftco and SCM orders comes with ill grace.

In its principal brief (SCM Br. 36-46), SCM argued that it was an unconstitutional denial of due process for the Commission to impose on SCM a more severe cease and desist order than on Kraftco, which committed the exact same violation, just because SCM chose to exercise its due process right to a hearing while Kraftco capitulated to a consent cease and desist order. The Commission responded to this argument by taking the position that, because SCM was an "adjudged . . . violator of Section 8 . . . and Section 5" while Kraftco "settled its differences with the Commission without litigation", the two orders cannot be compared (FTC Br. 32).

The Commission's argument exalts form over substance. How can the Commission seriously contend that the public interest requires issuance of a substantially harsher cease and desist order on one of two corporations, sharing a com-

mon director who is thereby in violation of Section 8, just because one corporation by exercising its constitutional right to a hearing caused the Commission to spend more time and money than did the other corporation that elected not to exercise its constitutional rights? Certainly it is not open to the Commission to contend that the Kraftco consent order saved it the risk of trying a doubtful case. (See Opinion of the Commission, p. 15, A163). On the FTC's theory of the case, the same stipulated record (A62-116) used to prove SCM's violation could also have been used to prove the same violation by Kraftco. In short, there are no meaningful differences between Kraftco's and SCM's alleged violations but only in their respective orders which, SCM submits, can and must be compared to understand the extent to which the Commission has punished SCM for exercising its constitutional rights.

None of the specific points raised by the Commission in its brief can justify the disparity in treatment between Kraftco and SCM.

(1) The Commission cites *United Van Lines, Inc. v. United States*, 545 F.2d 613 (8th Cir. 1976) for the proposition that an agency "is not obligated to impose uniform sanctions in cases concerning similar violations of the law." (FTC Br. 33). Whatever relevance the *United Van Lines* analysis might have to cases involving "similar" violations of the law, it is beside the point here as the FTC's discriminatory treatment of SCM vis à vis Kraftco occurred in the same case involving the same violation.

(2) The Commission argues that SCM may not rely on cases such as *Ford Motor Co. v. FTC*, [1976] Trade Cases (CCH) ¶ 60,938 (6th Cir. 1976), *vacated on other grounds*, [1976] Trade Cases (CCH) ¶ 61,218 (6th Cir. 1976) because



"mere disparity between orders is not sufficient" as "[t]here must be a showing that substantial *competitive injury* would result. . . ." (FTC Br. 34). In so arguing, the Commission fails to realize that the "competitive injury" limitation discussed by the Court in *Ford* applies only to an application to open a consent order. [1976] Trade Cases (CCH) ¶ 60,938, at 69,117-118. SCM's position in this litigation is exactly the reverse—it is not seeking to open the Kraftco or Bond consent orders but is arguing that the litigated order imposed on it is discriminatory when compared with those consent orders. Therefore, any "competitive injury" limitation has no application here and the cases cited in SCM's principal brief (SCM Br. 44-46) squarely apply.<sup>13</sup>

(3) Finally, the Commission challenges the relevance of cases such as *North Carolina v. Pearce*, 395 U.S. 711 (1969), cited by SCM for the proposition that it is an unconstitutional deprivation of due process to discriminate against one of several identically situated respondents solely because that respondent chose to exercise its constitutional right to a hearing. (SCM Br. 41-44). Citing no authority, the Commission argues that "*Pearce*, and related cases cited by SCM, are limited to cases in which a party is penalized for exercising appellate remedies—[t]he cases do not concern situations in which parties demand and receive trials." (FTC Br. 36-37). Why the constitutional principles articulated in *Pearce*, *supra*, and its progeny should be restricted to appellate proceedings, as distin-

<sup>13</sup> The principal point of those cases is that the Commission has a duty to explain, by legally acceptable reasons, differences in treatment of similarly situated respondents. Here, the only reason offered by the Commission, that SCM's decision to exercise its constitutional rights required the Commission to expend extra "time" and "money", is constitutionally infirm. See SCM's principal brief at 41-44.



guished from trials, the Commission does not bother to articulate. The Supreme Court's concern in *Pearce* was that a "trial court" (395 U.S. at 723) might punish a defendant for having exercised constitutional, due process rights. It is true that, in *Pearce*, the exercise of those rights occurred in an appellate forum. But to suggest, as does the Commission, that the constitutional principle that one must not be punished for exercising constitutional rights is somehow limited to cases involving appeals is to confuse the facts of that case for its holding. Furthermore, in *Blackledge v. Perry*, 417 U.S. 21 (1974), the Supreme Court extended the constitutional rationale of *Pearce* to prosecutorial discretion in the context of a *de novo* trial. Suffice it to say that there is no reason why the *Pearce* rationale should not apply in an administrative setting, as recent cases have held. See *Dan J. Sheehan Co. v. Occupational Safety and Health Review Commission*, 520 F.2d 1036, 1040 (5th Cir. 1975), *cert. denied*, 424 U.S. 965 (1976).<sup>14</sup> See also, cases cited in SCM's principal brief at 44 n.34.

(4) One of the Commission's alleged justifications for imposing a harsher cease and desist order on SCM than on Kraftco is that the public interest is served by speedy resolution of controversies. (FTC Br. 37, citing Opinion of the Commission, p. 15, A163). If anything, that factor

<sup>14</sup> The Commission (FTC Br. 35-36 & n.30) accuses SCM of misciting *Sheehan*, *supra*, by failing to note the Court's statement that: "imposition of a more severe penalty following a successful appeal is not per se constitutionally infirm." (520 F.2d at 1040). Of course, the Court also said: "If the Commission does not offer any reason for its decision to increase or if there is evidence that the increase was designed to penalize the employer for exercising its right to contest, the court will be in a position to correct such an abuse of discretion." (520 F.2d at 1041-42). Here, the only reason given by the Commission for imposing a harsher order on SCM than on Kraftco is that SCM caused the Commission to spend "time" and "money" by exercising its rights to a hearing. (A163)

should have led to a less severe order against SCM as SCM quickly entered into a Stipulated Record (A62-116), saving the Commission the added "time" and "money" required to prove that a violation had occurred. Moreover, SCM's refusal to submit to an unjustified cease and desist order has served the broader public interest in obtaining higher court review of important legal questions—such as the propriety of the Commission's admitted practice of routinely issuing cease and desist orders without any showing of a "cognizable danger of recurrent violation" and the applicability of Section 8 to corporations.

### CONCLUSION

SCM respectfully asks this Court to grant its petition for review, to vacate the Commission's cease and desist order and to dismiss the Commission's complaint against SCM.

Dated: New York, New York  
July 25, 1977

Respectfully submitted,

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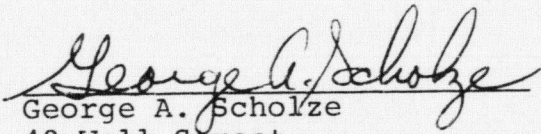
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CERTIFICATE OF SERVICE

Service of two copies of the annexed brief was made upon the Respondent herein by placing same in the United States mail, postage prepaid, this 25th day of July, 1977 directed to:

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